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# Article 9: What It Does for the Past

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## ARTICLE 9: WHAT IT DOES FOR THE PAST

*Grant Gilmore\**

### I

Article 9 is said to be the most novel, even the most revolutionary, part of the Code. This is a good deal more nearly true of its form than of its substance. Like any statute, it stands firmly rooted in the past, peering uncertainly toward the future.

In my first lecture I shall talk mostly of what the article accomplishes — its relatively satisfactory resolution of past controversies. In the second lecture I shall be mostly concerned with what the article does not accomplish — with the questions it does not answer and the problems it does not solve. Today we shall look backward, which is no great trick. Tomorrow we shall look, as through a glass darkly, toward what lies ahead.

Perhaps I should start with a word of explanation — not of apology — for taking up half my time with you in merely tracing the road along which we have come to get to where we are. Surely the principal function of a Code is to abolish the past. At least a common lawyer assumes that that was the theory on which the great civil law codes were based. From the date of the Code's enactment, the pre-Code law is no longer available as a source of law. The gaps, the ambiguities, the unforeseen situations cannot be referred for decision to the accumulated wisdom of the past. There is a fresh start, a new universe of legal discourse, in which the only permissible way of solving a problem is to find (or pretend to find) the answer in the undefiled, the unconstrued, the uncontaminated text of the Code itself. How well the theory worked in practice, or whether it worked at all, you, as civilians, are much better equipped to say than I.

The Uniform Commercial Code, so-called, is not that sort of Code — even in theory. It derives from the common law, not the civil law, tradition. We shall do better to think of it as a big statute — or a collection of statutes bound together in the same

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book — which goes as far as it goes and no further. It assumes the continuing existence of a large body of pre-Code and non-Code law on which it rests for support, which it displaces to the least possible extent, and without which it could not survive. The solid stuff of pre-Code law will furnish the rationale of decision quite as often as the Code's own gossamer substance.

The idea of using personal property as security for debt in any other way than by its simple delivery in pledge is not an old one. We need look no further back than the first half of the nineteenth century for the filing statutes which authorized mortgages of chattels with the mortgagor remaining in possession throughout the loan period or until default. The only statutory contribution at this point was the establishment of a filing or recording system under which public notice of the mortgagee's interest through a public record was substituted, as a validating or perfecting device, for the pledgee's traditional possession. The development of the substantive content of the new law of nonpossessory security interests in personal property was left to judicial improvisation. No doubt it was assumed, to the extent that anyone gave thought to the problem, that the law of real property mortgages and the law of pledge would provide the necessary guides of helpful analogy. But a mortgage of Black-acre presents problems quite different from those presented by a mortgage of a business enterprise's equipment, inventory or receivables. And property safely in a pledgee's possession is not at all the same thing as the same property in the borrower's possession. The analogies drawn from the law of pledge and mortgage proved to be feeble reeds to lean on.

We are accustomed to the idea that the nineteenth century attempt to create a stable structure of personal property security law by judicial, as opposed to legislative, fiat had, by the end of the century, foundered in an immense confusion. The attempt failed, it is true, but it came close to succeeding. Except for one controversy, which was never resolved within the framework of the nineteenth century structure, it quite probably would have succeeded.

In *Swift v. Tyson*,<sup>1</sup> Justice Story announced the doctrine of a general federal commercial law, independent of state law. In this, as in many of his other great decisions, Story was the apostle — with a little more luck, he could have been the archi-

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1. 41 U.S. (16 Pet.) 1 (1842).

test — of a nationally uniform commercial law. We know of *Swift v. Tyson* only in its disreputable old age — a toothless and unlovely hag. We forget that for half a century or more the doctrine of the general federal commercial law worked very well indeed. Even the discovery, which was made twenty years or so after the doctrine was promulgated, that the federal courts were bound by state statutes even though they were not bound by state decisional law, made very little difference, since commercial law on any level remained uncoded well into this century.

In those days the Supreme Court of the United States was a great commercial court and, under its guidance, the lower federal courts did their work well. It was the Supreme Court which established the effectiveness of after-acquired property clauses in corporate financing — first in railroad mortgages and later, as the court put it, “in other similar great and important enterprises of the day.”<sup>2</sup> It was the Supreme Court which later worked out the intricate matter of the priority for purchase money financing over the after-acquired property interest: once again the progression was from the financing of railroad equipment — the rolling stock — to the financing of industrial equipment used in connection with, or affixed to, real property.<sup>3</sup> And even after the turn of the century it was a pair of Supreme Court cases which set the pattern for the odd variant of inventory financing which came to be known as field warehousing.<sup>4</sup>

In the several illustrations I have given you of the creative role which the Supreme Court played in the development of personal property security law from 1850 until after 1900, the court did not announce — or did not quite announce — what today we would call a rule of federal law. It was, in fact, dealing with issues which the state courts had wrestled with inconclusively. It was imposing — or suggesting — a pattern of order to replace the prevailing chaos. There are intimations in some of the opinions that if an overriding rule of federal law were needed, the

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2. See *Pennock v. Coe*, 64 U.S. (23 How.) 117, 130 (1860).

3. The basic railroad case was *United States v. New Orleans R.R.*, 79 U.S. (12 Wall.) 362 (1871). The two leading Supreme Court cases on industrial equipment financing were *Holt v. Henley*, 232 U.S. 637 (1914); *Detroit Steel Cooperage Co. v. Sistersville Brewing Co.*, 233 U.S. 712 (1914). The developments briefly referred to here are reviewed in 2 GILMORE, *SECURITY INTERESTS IN PERSONAL PROPERTY* c. 28 (1965). An earlier version of the chapter referred to appeared as *The Purchase Money Priority*, 76 HARV. LAW REV. 1333 (1963).

4. *Union Trust Co. v. Wilson*, 198 U.S. 530 (1905); *Security Warehousing Co. v. Hand*, 206 U.S. 415 (1907).

rule would be forthcoming. But the court seems to have been sensitive to the felt needs of the time. It led and the state courts, with the state legislatures not infrequently playing a supporting role, followed.

To this pattern of a smooth and orderly development, there was one major exception — one issue which found the state courts arrayed in opposing camps and the federal courts unable to produce a solution around which a new consensus could form. The failure to resolve this single issue eventually brought the whole structure crashing down.

The point of breakdown was the apparently simple problem of devising a satisfactory method of financing on the security of a merchant's stock in trade or a manufacturer's inventory. From the beginnings — that is, from 1830 to 1840 — one group of state courts held that inventory mortgages were necessarily, and as matter of law, fraudulent. Another group of courts held that, in the absence of a showing of actual fraud or dishonesty, such mortgages represented entirely legitimate transactions. In the 1870's the Supreme Court of the United States, aligning itself with the "fraud in law" forces, announced what sounded suspiciously like a federal fraud in law rule, but, on this occasion, the Justices were evidently out of touch with the real world and not even the lower federal courts paid the least attention to what they said.<sup>5</sup> By the end of the century it had become a popular sport with the writers of chattel mortgage treatises — of which there were many — to draw up lists of "fraud in law" states and "fraud in fact" states. If the treatise writer looked on the inventory mortgage as a wicked engine of fraud, his list would show a great many fraud in law states and only a few fraud in fact states. If he found the inventory mortgage to be a useful and praiseworthy financing device, his list would show that the fraud in fact states far outnumbered the few states which still clung to the discredited fraud in law doctrine.<sup>6</sup> No-

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5. The Supreme Court "fraud in law" case was *Robinson v. Elliott*, 89 U.S. (22 Wall.) 513 (1874). In *Brett v. Carter*, 54 Fed. Cas. 67 (D. Mass. 1875), Lowell, J., remarked that he doubted "both the generality and the justice of the doctrine" of *Robinson v. Elliott*. In later cases the Supreme Court itself receded from the position it had apparently taken in *Robinson v. Elliott*. Michigan and Iowa rules under which stock in trade mortgages were valid were approved in *Peoples Savings Bank v. Bates*, 120 U.S. 556 (1887) (Michigan); *Etheridge v. Sperry*, 139 U.S. 266 (1891) (Iowa).

6. See JONES, MORTGAGES OF PERSONAL PROPERTY § 415 (4th ed. 1894); PIERCE, FRAUDULENT MORTGAGES OF MERCHANDISE, cc. 3-7 (1892); 1 COBBEY, CHATTEL MORTGAGES § 309 (1893).

body could be sure of anything and inventory financing in any state was a doubtful gamble.

But what was the fraud? The underlying idea — which derived quite directly from a decision of the Star Chamber in 1601, reported by Lord Coke as *Twyne's Case*<sup>7</sup> — was that there was a fraud on creditors if the mortgagor was not only left in possession of the mortgaged property but was allowed to use it as if it were his own. That meant, in the context of an inventory mortgage, that the mortgage was fraudulent if the mortgagor was allowed to sell the stock in the ordinary course of his business without being under a duty to account to the mortgagee for the proceeds of sale. It is only by an accident of history or journalism that the word "fraud" got mixed up with all this. A more neutral term like "invalid against creditors" would very probably have simplified both the debate and the solution.

The solution, when it came, was the discovery, invention, or spontaneous germination of a whole host of what we may call inventory security devices — all of which begin to appear in the case reports around 1900, all of which are alike in that their principal claim to fame is that they are not chattel mortgages. Some of these devices — like the security consignment — lodged on barren ground, struggled for awhile and disappeared. Others took root and flourished. Presently we had the trust receipt, the factor's lien, and the field warehousing pledge — and what appeared to be a new era in personal property security law, a sort of late Byzantine era in which complexity for its own sake became the craftsman's aim.

In time all these new devices, except the field warehousing pledge which for a time escaped the common fate, passed under the statutory yoke, were equipped with filing systems, had their boundaries sharply defined, and acquired each its own distinctive theology and ritual. The codification, if we should call it that, of the personal property security devices was merely a part of the general tendency, which established itself before World War I and proceeded at a rapidly accelerating pace thereafter, to replace decisional law with a statutory formulation.<sup>8</sup> A peculiarly fascinating example of that tendency is found, I suggest, in the compulsion which induced the authors of the

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7. 3 Co. Rep. 806, 76 Eng. Rep. 809 (Star Chamber, 1601).

8. See Gilmore, *Legal Realism: Its Cause and Cure*, 70 YALE L.J. 1037 (1961).

so-called Restatements to reduce to black-letter text even those segments of the common law which had remained uncoded.

The coming of the statutes marked the end of the once promising attempt to build a nationally uniform system of commercial law under the superintendence of the federal judiciary. Perhaps the attempt would have failed in any case. At all events the well-meant and largely successful labors of the National Conference of Commissioners on Uniform State Laws had, as one of their incidental effects, the reduction of the doctrine of *Swift v. Tyson* to the state of toothless decrepitude we have previously deplored. The federal courts went out of the commercial law business, apparently for good — although there is a modern sequel which we will come across tomorrow.

We must return from our digression about statutes to pick up the thread of our story, which we left with the dramatic emergence of the inventory security devices. That extraordinary solution of the great nineteenth century controversy was achieved at the considerable cost of a fragmentation of security law into a thing of bits and pieces. However, no matter how great the price that must be paid, no war is ever really won. Today's great victory is merely the prelude to tomorrow's grim campaign. And so it was that when the financial community, after a fifty year struggle, had reached the point where it had become possible to make working capital loans safely on the security of inventory, it suddenly became apparent that inventory financing — except in a few situations, such as automobile distribution — was not really desirable after all. Much better than inventory, as security, were the receivables which arose when the inventory was sold. That is an obvious proposition, as soon as it is stated: if the borrower's default or insolvency is assumed, the unsold inventory will in all probability be worthless; the receivables need only be collected. The baffling point is why we hear nothing of anything like institutionalized receivables financing much before the 1920's. No doubt banking, like law, has its own impenetrable mysteries.

Financing on the security of receivables — the short-term receivables which arise when goods are sold or services rendered on credit — presented exactly the same problem in the 1920's that financing on the security of inventory had presented in the 1870's. The controversy over receivables was an almost exact replay — a sort of revival — of the controversy over the stock

in trade mortgage. This time, however, the show, instead of running for half a century, closed almost as soon as it opened. The United States Supreme Court settled the issue in what proved to be its last significant contribution to security law. In *Benedict v. Ratner*,<sup>9</sup> in which Justice Brandeis' opinion relied almost exclusively on the nineteenth century stock in trade mortgage cases, the Court set aside in a bankruptcy proceeding a receivables financing arrangement in which the assignor was allowed to make collections of the assigned receivables and use the proceeds for his own purposes without accounting for them to the assignee.

In 1925, when the *Benedict* case was decided, an informed observer might have predicted that what later came to be called non-notification accounts receivable financing was dead. After *Benedict* the only type of receivables financing that might have seemed possible was one which had grown up in the textile industry and was known as "factoring." Textile factoring had in its origins been inventory financing but had evolved into a straight receivables arrangement. The accepted pattern was that the invoices for goods shipped from the mill went out over the factor's letterhead and the buyers or account debtors paid the factor-assignee. Thus the money never got into the hands of the mill owner-assignor, so that the arrangement was not vulnerable under *Benedict* theory.

Our hypothetical observer would have been completely wrong in his prediction. The so-called factoring arrangement did not by any means disappear: it is still with us, it is no longer confined to the textile industry, and it accounts for a volume of several billion dollars worth of financing a year. But what happened, during the period after 1925, was a sensational growth in non-notification receivables financing—that is, arrangements in which the assignor continues to make the collections from the account debtors, who are not notified that the accounts which they owe have been assigned.<sup>10</sup> The post-*Benedict* arrangements of this sort were, however, carried out in such a way that the assignor was not allowed to exercise the "unfettered dominion"

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9. 268 U.S. 353 (1925).

10. It has been estimated that in recent years the annual volume of financing done under "factoring" arrangements has been in the neighborhood of four billion dollars and that the annual volume of non-notification accounts receivable financing has been in the neighborhood of six billion dollars. Comment, *Multistate Accounts Receivable Financing: Conflicts in Context*, 67 YALE L.J. 402, 404, n.16 (1958).



over the assigned accounts which Justice Brandeis had stigmatized as fraudulent. The accepted technique for complying with the rule in *Benedict* was the use of a so-called revolving credit. Strict accountability was imposed on the assignor, who was required to remit all collections to the assignee as they were received — it is true that they were immediately, in the jargon of the trade, re-remitted to the assignor. A constant ratio was maintained between collateral and debt: if the aggregate value of the assigned receivables decreased by twenty per cent, there had to be a proportionate pay-down on the loan.<sup>11</sup>

The complicated pattern of receivables financing which I have just described bore a quite startling resemblance to the techniques of inventory financing which had become customary under the two most successful inventory security devices — the trust receipt and the field warehousing pledge. In trust receipt financing and in field warehousing, the borrower was held to the strictest accountability. The most elaborate controls were set up to insure that the automobile dealer did not sell his trust-receipted cars out of trust — that is, without immediately remitting the proceeds to the entruster — and that the borrower did not withdraw goods from the field warehouse without making a proportionate payment on the loan. The controls were not, of course, always successful; the cars were sold out of trust and the field warehouse was often empty when the holder of the warehouse receipts came to look for his collateral. The reason why you set up controls in the first place is that you know you are operating in an area where fraud is endemic and inevitable. If you have the bad luck to lend thirty million dollars to an unusually determined and ingenious crook, the controls will do you no good and there will be no soy-bean oil in the tanks when you go out to the New Jersey tank farm to look.

The specialists in inventory and receivables financing never suggested that the rules they operated under should be relaxed. This became clear during the 1940's when, for reasons which are not germane to our discussion, most states enacted statutes which regulated the assignment of accounts receivable. The political situation was such that there is no doubt whatever that the finance companies, who by this time were doing a large volume of non-notification receivables financing, could have per-

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11. Good examples from the recent case law of "how to comply with the rule in *Benedict*" are *In re New Haven Clock & Watch Co.*, 253 F.2d 577 (2d Cir. 1958); *Steven v. Union Trust Co.*, 316 F.2d 687 (D.C. Cir. 1963).

suaded the state legislatures to include in the accounts receivable statutes provisions repealing the *Benedict* rule. They made no attempt to do so. They had, it appears, become the most ardent twentieth century supporters of the underlying principle which runs from *Twyne's Case* through the nineteenth century inventory mortgage cases to its ultimate formulation in *Benedict v. Ratner*.

A student's first reaction to a study of personal property security law during the first half of this century is that the fall of the Roman Empire must have been much the same sort of thing. There appears to be a process of disorganization, dissolution, disintegration at work. With the appearance of each new independent security device, with the piling of each new statute on the untidy heap, the picture appears to grow more confused and more obscure. I shall suggest, however, that the apparent triumph of a truly barbarous diversity concealed, for a time, the edification of a remarkably unified structure of law — as a scaffolding conceals a building in course of construction.

I have already commented on the startling similarity of the patterns or techniques that emerged both in inventory and receivables financing. I shall cite another example of the unity-in-diversity theme, which is even more dramatic. In most states, during the nineteenth century, the conditional sale or an analogous device had appeared as a competitor to the older chattel mortgage. In its origins the conditional sale, or sale on condition, derived from a conceptual system which had no contact whatever with mortgage theory; indeed the conditional sale was not, to start with, a security device at all. As we came down into this century, the two competing devices almost everywhere merged and fused. Where the conditional sale was not turned into the equivalent of the chattel mortgage by legislation, it gradually became so by a case law development. All that remained to distinguish them was the terminology and the unfortunate fact that, although in most states both the conditional sale contract and the chattel mortgage had to be filed, they were usually filed in different books, set up according to different theories, and kept in different places. Indeed the multiplication of filing systems, which we might with a degree of paradox describe as both unnecessary and inevitable, was the one really annoying feature of the state of security law which had been achieved by mid-century.

I should also like to draw to your attention one significant result of the historical process which I have been describing and distorting for you during the past half hour. That is, that financing on the security of the short-term or liquid assets — the inventory and receivables — of a business enterprise had become permanently divorced from financing on the security of the long-term or fixed assets — the plant and equipment. After 1910 or so, the security for the bonds issued under the typical corporate indenture never included the inventory or the receivables. Those short-term, liquid, and highly volatile assets went up as security for working capital loans made by specialists under the complicated procedures of revolving credits and the like. Those procedures guaranteed that the lender who took such dangerous and doubtful collateral as security would keep a close watch on his borrower's affairs — would be, in the odd term which came into use, the borrower's policeman.

I started by saying that article 9 has been described as a revolutionary departure and went on to comment that the description was more apt with respect to the article's terminology, which is novel, than with respect to its substance, which is not. Perhaps, in law as in politics, what appears to be a revolution is merely the recognition *de jure* of what has long since taken place *de facto*. All the article 9 draftsmen really had to do was to tear down the scaffolding and reveal the building. Their only real contribution, which was simple, obvious, and as easy as rolling off a log, was to substitute a single filing system for the half-dozen systems which had grown up in most states under the pre-Code security statutes.

Naturally, the draftsmen — I happened to be one of them — did not, when they set about their task in the late 1940's, see matters in quite that clear, Olympian light. While you are climbing the mountain, you are greatly impressed at your own fortitude and ingenuity in overcoming obstacles. When you reach the top, the thought may occur to you that you really haven't come so far after all.

The basic idea for what became article 9 had apparently occurred independently to several of us. That was that there should be a single, comprehensive statute which would cover all types of personal property security transactions, regardless of the form in which they were cast. Instead of chattel mortgages, conditional sales, trust receipts, and so on, there was to be a

unitary "security interest" in personal property, tangible and intangible. The original project, however, contemplated a five-part division of the statute according to what were conceived to be significantly different types of financing transactions. In early drafts, therefore, there were separate parts on Inventory and Accounts Receivable Financing; Industrial Equipment Financing; Agricultural Financing; Consumer Goods Financing; and Pledge. Indeed, a sixth part, on long-term contract rights financing as distinguished from short-term accounts receivable financing, was projected but never reached draft stage. As the early drafts progressed, each of the separate parts tended to become more and more nearly a Chinese copy of each of the other parts. Evidently the assumption that there were significant differences in the various types of financing transactions which had been singled out for separate treatment had been erroneous. Finally the original scheme of organization was scrapped and the article was redrafted as a single unit. The division into five parts remained, but the parts now dealt with such matters as Formal Requisites, Attachment and Perfection, Priorities, Filing and Default. The only residue from the original plan was the retention of an elaborate series of definitions which classify all types of personal property into four categories of goods — inventory, equipment, farm products, and consumer goods — three categories of what might be called pledgeable intangibles — instruments, documents, and chattel paper — and three categories of pure or non-pledgeable intangibles — accounts, contract rights, and general intangibles.<sup>12</sup> The original drafting scheme had required most of this complicated classification. When the structure of the article was simplified, most of the categories could have been dropped. Unfortunately, by that time the drafting staff had become so accustomed to finding its way through the definitional jungle that it never occurred to anybody that it would be helpful to simplify the terminology as well as the structure.

The simplest way of explaining what article 9 does is to say that it accepts the verdict of history. It provides that any type of personal property, tangible or intangible, can be used as collateral to secure a loan. It reduces to a minimum the formal requisites for creation of a security interest. It introduces a greatly simplified filing system. With respect to default rights, it adopts what had become the universal pattern of security law:

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12. For the definitions, see §§ 9-105, 9-106, 9-109.

the normal procedure on default is for the secured party to sell the collateral and apply the proceeds to the expenses of sale and satisfaction of the secured obligation; the debtor is entitled to any surplus and is liable for any deficiency.

One unanticipated consequence of the structure of the article was that it imposed on the draftsmen an enormously complex treatment of the problem of priorities among security interests. Take, for example, the financing of the acquisition of a million dollars worth of new equipment by a corporation which has already given a mortgage on all its plant and equipment, including all property to be acquired during the term of the mortgage. It will be impossible for the corporation to purchase the new equipment unless it can give the purchase money financier a security interest which has priority over the claim of the bondholders under the after-acquired property clause of the mortgage. Under pre-Code law, the purchase money priority was worked out by a juggling manipulation of lien and title theory. The new equipment was financed under a title-retention device — the conditional sale or the so-called equipment trust. The result was priority for the purchase money financing — the new money — since (or so the conceptual explanation ran) title to the new equipment was never transferred to the mortgagor corporation and therefore there was nothing for the lien of the mortgage to attach to. The article 9 draftsmen had no quarrel with the doctrine of purchase money priority but, having adopted the idea of a unitary security interest, there was no way of solving the problem by the pre-Code title-lien distinction.<sup>13</sup> The problem had to be handled as one of priorities between after-acquired property interests and purchase money interests (which required still another definition of what a "purchase money security interest" was).<sup>14</sup> I am afraid that the draftsmen, having whetted their appetite on a few obvious priority problems like that of purchase money financing, went on to devour all the priority problems in sight and a few more that had never been seen or even imagined before. After awhile priorities get to be an addiction like cocaine or heroin.

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13. Section 9-202 provides: "Each provision of this Article with regard to rights, obligations and remedies applies whether title to collateral is in the secured party or in the debtor."

14. For the definition of "purchase money security interest," see § 9-107. The priorities between purchase money and non-purchase money security interests are worked out in § 9-312(3), (4).

Article 9 contains the most forthright repealer of the dominion rule of *Benedict v. Ratner* which the wit and industry of the draftsmen could put together.

Section 9-205 provides that:

"A security interest is not invalid or fraudulent against creditors by reason of liberty in the debtor to use, commingle or dispose of all or part of the collateral (including returned or repossessed goods) or to collect or compromise accounts, contract rights or chattel paper, or to accept the return of goods, or to use, commingle or dispose of proceeds, or by reason of the failure of the secured party to require the debtor to account for proceeds or replace collateral."

Clearly the draftsmen were not niggardly in their use of words — the sentence rolls on like some great Niagara of jargon — but there can be no doubt that, after three hundred and sixty-odd years, *Twyne's Case* is dead as a doornail.

But who wanted to kill *Twyne's Case*? A little earlier I described the inventory and receivables financing patterns whose use is thought to have been compelled by the theory of *Twyne's Case* and its twentieth century reformulation in *Benedict*. I assume that I left you with the impression that I thought they were good and desirable patterns. I also commented on the fact that during the 1940's the finance companies, which had become the leading specialists in both inventory and receivables financing, made no attempt to have the rule in *Benedict* repealed when they could easily have done so. In this instance we know perfectly well who killed Cock Robin. The question is: why did they?

As one of the murderers, now getting on in years, I sometimes wonder — sitting before my fire in the evening — whether what we did was quite right. No doubt the regicide judges who signed the death warrant for King Charles I put similar questions to themselves in later years. It was a difficult situation. There were many arguments both ways. Perhaps a less extreme solution might have worked. Perhaps not.

There are two thoughts which somewhat console me.

One is that it is not unreasonable to say that article 9 abolishes the dominion rule only in its formal aspects and preserves its substance. Closely related to the *Benedict* repealer which I have read to you is a complicated provision, which I shall not

read to you, in section 9-306 which deals with a secured party's right to "proceeds" — the receivables which arise when inventory is sold and the money which comes in when the receivables are collected. These are the direct or immediate security in receivables financing and the real security — the only source from which the lender will ever be repaid — in inventory financing. The section 9-306 proceeds provision says in substance that if insolvency proceedings are instituted against the debtor, the only proceeds which the secured party can claim are those which the debtor received during the ten days preceding the institution of the proceeding less whatever was actually paid over to the secured party during the same period. Thus, in the one contingency where the secured party will need his collateral, section 9-306 puts beyond his reach anything he has allowed the debtor to keep and use for more than the ten days before bankruptcy day. The Code secured party thus is provided with a considerable incentive to continue the policing practices which his pre-Code counterparts developed.

The second thought which consoles me is that, if all speed limits were removed on the highways, it does not necessarily follow that people will start driving at 100 miles an hour along winding, two-lane country roads. The repealer of *Benedict*, the murder of *Twyne's Case*, were acts decided upon after lenders had had fifty years of experience in finding out how security-like inventory and receivables ought to be handled. No professional whom I have talked to in the last fifteen years has ever expressed the slightest interest in taking advantage of the Code's lowering of barriers. Once a policeman, always a policeman. The danger is, of course, that amateurs may be tempted to get into the act — although that does not seem to have happened, to any appreciable extent, in the states which have lived with the Code for up to ten years.

I noted earlier that one of the odd results of our history was the divorcement of long-term financing on the fixed assets of an enterprise from short-term financing on the security of its inventory and receivables. Under article 9 the divorcement is no longer required as matter of law. There is nothing to prevent the draftsman of corporate indentures in Code states from reaching out to cover the inventory and receivables as well as the plant and equipment. There is no reason why they should and it should be remembered that, if they were to do such a thing, the bondholders would take subject to the priority for subsequent

purchase money interests in both equipment and inventory as well as to the limitation on a proceeds claim in insolvency proceedings. I will admit, however, that this possibility worries me more than the idea that amateurs will start making unpoliced inventory and receivables loans. I think that the divorcement between long-term and short-term financing, with the segregation of the fixed assets from the quick assets, has been a desirable feature of our security law, no matter for what strange reasons it was arrived at. I have come to feel that, with a little more ingenuity or a better reading of history, we might have done more than in fact we did to preserve this remote descendant of *Twyne's Case*.

Article 9 is sometimes described as a "floating lien" statute. In common law parts, those are, or once were, fighting words — although people seem to be getting used to the idea that it is respectable for a lien to float in the United States, as it has long done in England and Canada. Insofar as "floating lien" is a meaningful term, the reference is principally to those aspects of the article 9 security interest which we have mentioned: the validation of the after-acquired property interest and the repeal of the rule of *Benedict v. Ratner*. Article 9 does make it possible for a lender to take a security interest in all of a debtor's present and future property, advance his money, sit back and take no further interest in what goes on. He will not be well advised to do this. This hypothetical course of action makes little or no sense from a business or banking point of view. Furthermore, it makes no sense because of some interesting and curious developments connected with the surprising rebirth of the general federal commercial law which we left for dead some time back.

But that will be a part of our discussion tomorrow.